

**LEGISLATIVE SERVICES AGENCY  
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS**

200 W. Washington, Suite 301  
Indianapolis, IN 46204  
(317) 233-0696  
<http://www.in.gov/legislative>

**FISCAL IMPACT STATEMENT**

**LS 6905**

**BILL NUMBER:** HB 1755

**NOTE PREPARED:** Jan 11, 2007

**BILL AMENDED:**

**SUBJECT:** Adjusted Gross Income Tax.

**FIRST AUTHOR:** Rep. Davis

**FIRST SPONSOR:**

**BILL STATUS:** As Introduced

**FUNDS AFFECTED:** X GENERAL  
X DEDICATED  
FEDERAL

**IMPACT:** State & Local

**Summary of Legislation:** The bill exempts active duty military pay earned by members of the National Guard and Reserves from the Individual Income Tax. It provides that a taxpayer may not claim both the new exemption and the existing deduction for military income. It also increases the amount of the existing deduction from \$2,000 to \$5,000 for service in an active component of the armed forces of the United States.

**Effective Date:** January 1, 2008.

**Explanation of State Expenditures:** The Department of State Revenue (DOR) will incur additional expenses to revise tax forms, instructions, and computer programs to reflect the deduction changes relating to active duty military pay. The DOR's current level of resources should be sufficient to implement these changes.

**Explanation of State Revenues:** *Summary:* The bill would reduce state Adjusted Gross Income (AGI) Tax liabilities of individual taxpayers who are on active duty. The revenue loss from the bill could potentially total \$2.4 M to \$2.7 M in FY 2009, with the revenue loss increasing by about 1.5% annually thereafter.

*Background Information:* The bill provides: (1) a full exemption for active duty pay earned by Armed Forces Reserve and National Guard members in lieu of the current \$2,000 exemption.; and (2) increases from \$2,000 to \$5,000 the deduction for active duty military personnel. (Note: Currently, combat pay is excluded from federal gross income and, as a result, is excluded from state AGI.) Since the bill is effective beginning in tax year 2008, the fiscal impact would begin in FY 2009. Eighty-six percent of the revenue from the AGI Tax on individuals is deposited in the state General Fund, and 14% of the revenue is deposited in the Property Tax Replacement Fund.

Under current statute, a taxpayer may deduct up to \$2,000 in military service income from state AGI. This includes military retirement, provided the recipient is 60 years old or older. State tax data indicates that 36,530 taxpayers claimed the deduction for military service pay and retirement benefits in tax year 2004, deducting approximately \$72.5 M in military pay and retirement benefits. This amount resulted in a revenue loss of about \$2.5 M. Based on U.S. Department of Defense military census and pay rate data, it is estimated that about 35% of the annual total amount deducted under the current \$2,000 deduction is attributable to Indiana taxpayers earning active duty pay during the year. The changes made by the bill would increase the total annual active duty pay deducted from AGI by about \$73 M to \$79 M in tax year 2008, with a tax impact of about \$2.4 M to \$2.7 M.

**Explanation of Local Expenditures:**

**Explanation of Local Revenues:** Because the proposed increase in the military service income deduction would decrease taxable income, counties imposing local option income taxes (CAGIT, COIT, and/or CEDIT) may, as a result, experience an indeterminable decrease in revenue from these taxes.

**State Agencies Affected:** Department of State Revenue.

**Local Agencies Affected:** Counties with local option income taxes.

**Information Sources:** OFMA Income Tax databases, 1996-2004; Deborah K. Williamson, U.S. Department of Defense, Defense Manpower Data Center, (831) 583-2400; Matthew Torres, U.S. Department of Defense, Defense Manpower Data Center, (831) 583-2500; Capt Lisa Kopczynski, Indiana National Guard; MSG Chris Poore, 317-964-7053, Army Personnel; SGT Shunt; <http://arc.publicdebt.treas.gov/DWP/fs/fshudagebands.htm>.

**Fiscal Analyst:** Jim Landers, 317-232-9869.